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Robert Haga
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March 25, 1999

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APR 01 1999
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Magalie Roman Salas
Secretary
Federal Communications Commission
445 12th Street, S.W.
12th Street Lobby, TW-A325
Washington, D.C. 20554

RE: Revision to the Methodology for Allocating Costs Among the Four Universal Service Support Mechanisms that was filed on December 31, 1998 **(CC Docket Nos. 97-21 and 96-45)**

Dear Ms. Salas:

On December 31, 1998, the Universal Service Administrative Company (USAC) filed a method for allocating costs to each of the four Universal Service support mechanisms, in compliance with the Commission's November 20, 1998 Order.[1] USAC subsequently filed a report with the Commission on March 5, 1999 in response to the Commission's directive to evaluate the rural health care program and to submit a report that included decreased administrative costs. As part of that evaluation we reviewed the method for allocating common costs and the report recommends a change to the allocation of common compensation costs.

We proposed that several of the Common costs are more appropriately allocated based on program size rather than direct costs allocated to each program. The changes to the December 31, 1998 filing are enclosed with this filing.

In accordance with Commission rules, I am submitting two copies of this notice for each docket to the Office of the Secretary. Please acknowledge receipt hereof by affixing a notation on a duplicate copy of this letter furnished herewith for such purposes and remitting same to the bearer.

Sincerely,

Robert Haga

RH:cah:\letters\FCC\Salas cost allocation 399

Enclosures
cc: Lisa Zaina, FCC
Irene Flannery, FCC

No. of Copies rec'd 0+4
List A B C D E

[1] Changes to the Board of Directors of the National Exchange Carrier Association, Inc. and Federal-State Joint Board on Universal Service, Third Report and Order and Fourth Order on Reconsideration and Eighth Order on Reconsideration, CC Docket Nos. 97-21 and 96-45, FCC 98-306, released on November 20, 1998 at ¶61 ("FCC Order").

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REVISIONS TO THE METHOD FOR ALLOCATING COSTS
April 1, 1999

Definition of Apportionment Factors
Add the following factor:
Program Size – The ratio of the size of the fund for each program to the total demand (size) for all four programs.
Eliminate the following factor:
Total Direct Dollars Assigned to Each Programmatic Area – The ratio of all dollars directly allocated to each programmatic area to the total of all directly allocated dollars (USAC and vendor dollars combined). Quarterly budget information is used for interim allocations and actual quarterly information is used for final allocation.

Common Expense Categories and Apportionment Method
Change the allocator as follows:
Accounting and General Financial Services From the Total Direct Dollars Assigned allocator to the Program Size allocator.
Audits - From the Total Direct Dollars Assigned allocator to the Program Size allocator. Programmatic audits will continue to be directly assigned.
Billing and Collection - In the March 5, 1999 Report to the FCC and Evaluation of the Rural Health Care Program USAC proposed that FCC take action to revise its May 1999 order which allocated Billing and Collections costs from 25% to each program to the Program Size allocator.[1] We would revise our Method for Allocating Costs at that time if the Commission adopts this recommendation.
Directors Officers (D&O) Liability Insurance – From the Total Direct Dollars Assigned allocator to the Program Size allocator.
Legal and Regulatory - From the Total Direct Dollars Assigned allocator to the Program Size allocator. Specific project work, however, will continue to be directly assigned.
Payroll and Employee Benefits - From the Total Direct Dollars Assigned allocator to the Program Size allocator.
Telephone Service – All charges that are common in nature shall be based on the Program Size allocator.
Vendor Outreach - From the Total Direct Dollars Assigned allocator to the Program Size allocator.
Miscellaneous - All other common costs that are not included above will be based on the Program Size allocator.

Assets and Liabilities
Assets and Liabilities that are common in nature will be allocated based on the Program Size allocator.

[1] Letter from Robert Haga to Magalie Sallas on March 5, 1999, Filing of Rural Health Care Evaluation Report in Response to Public Notice (CC Docket Nos. 96-45 and 97-21).

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METHOD FOR ALLOCATING COSTS

This document provides the proposed method for allocating costs among the four support mechanisms as directed in the Federal Communication Commission's Order.[1] This method provides a fair and reasonable procedure for allocating costs between each of the four universal service mechanisms: high cost, low income, rural health care, and schools and libraries. To the extent that costs can be directly attributed to a specific mechanism, those costs will be directly assigned. To the extent that the function benefits more than one of the programs, those common costs will be assigned based on an apportionment factor that reasonably allocates the costs associated with the common function.

The following procedures will be used to capture direct and common costs:

- The Budgeting Process
- Employee Time Sheets
- Purchase Requests
- Requests for Checks
- Journal Entries

In the plan of reorganization and in the Commission's Order it was recognized that some functions are appropriately consolidated and other functions were unique and should, therefore, remain as separate operations. The functions that will be consolidated will benefit more than one program and will fall into the category of common costs. The billing and collection function that is currently performed by USAC is a common function and will continue to be a common function after the merger. The Commission has approved the current allocation methodology for billing and collection and that method is incorporated into this document. USAC currently maintains the fund balances for all of the programs and those balances are allocated to each of the programs.

Those functions that will remain separate because they are unique to a particular program will be directly assigned to the specific mechanism. Those unique functions and costs will be budgeted by the divisions and reviewed by the respective board committees. Those functions and costs will be tracked separately in the accounting system and will be directly assigned to the appropriate mechanism.

Although the High Cost and Low Income programs will be included in one division budget and reviewed by one Committee, those budgets and costs will be directly assigned to each program or allocated as appropriate. The allocation procedures are currently in place for the High Cost and Low Income programs and will remain in place after the merger because a single division will administer these two programs. These procedures are also included in this document.

[1] Changes to the Board of Directors of the National Exchange Carrier Association, Inc. and Federal-State Joint Board on Universal Service, Third Report and Order and Fourth Order on Reconsideration and Eighth Order on Reconsideration, CC Docket Nos. 97-21 and 96-45, FCC 98-306, released on November 20, 1998 ("FCC Order").

Definition of Apportionment Factors

Employee Ratio – The ratio of full-time equivalent (FTE) staff dedicated to a particular activity to the total FTE staff dedicated to all activities (total company employees).

Square Feet Occupied – The ratio of square feet assigned to personnel or functions dedicated to a specific program to the total square feet occupied by those programs (excludes common space).

Relative Number of Visits to the Website – The ratio of the number of visits to each programmatic area of the website to the total of all the visits to all four programmatic areas. Monthly information is used for interim allocations and actual annual information is used for final allocation.

Total Direct Dollars Assigned to Each Programmatic Area – The ratio of all dollars directly allocated to each programmatic area to the total of all directly allocated dollars (USAC and vendor dollars combined). Quarterly budget information is used for interim allocations and actual quarterly information is used for final allocation.

Expenses that are Directly Assigned (Primarily those Functions Budgeted and Implemented at the Division Level)

Payroll and Employee Benefits - Employees assigned to the Rural Health Care and the Schools and Libraries divisions will be directly assigned to those programs. Exception reporting will be used if any of those employees are given special assignments to work on one or more of the other three programs. Employees assigned to the High Cost and Low Income division will be dedicated to a program function or a percentage of time will be allocated to each program based on an assessment of time spent on each program.

Client Outreach - Travel and mailings related to a particular beneficiary group will be directly assigned to each mechanism. Outreach by vendors that is related to a particular program will be assigned to that program.

Auditing - Audits of specific program functions and operations will be bid separately and directly assigned.

Program design and systems development - All programming and maintenance costs and the management of the system design will be directly assigned.

Client Support Centers - The cost of data systems, telephone systems, office supplies, and miscellaneous costs related to the support centers will be directly assigned.

Outside contractors - NECA will use its cost allocation manual to allocate costs between the programs. All other programmatic contracts will be program-specific or will require vendors to separately identify costs and assign staff to each programmatic area. Each outside vendor will be responsible for providing USAC with direct assigned dollars.

Taxes - All taxes will be charged directly to the program that generates the particular tax.

Uncollectibles - Uncollectibles will be directly charged to the appropriate mechanism.

Depreciation and Amortization - Depreciation and amortization will be charged to the appropriate mechanism. Depreciation and amortization charges that are common in nature shall be allocated 25% to each program.

Common Expense Categories and Apportionment Method
Payroll and Employee Benefits - Officers and administrative staff that perform common functions will be allocated based on the ratio of Total Direct Dollars Assigned to Each Programmatic Function.
Office Space - Total rentable space will be allocated based on square feet occupied.
Property and Liability Insurance - Insurance will be allocated based on square feet occupied.
Directors and Officers (D&O) Liability Insurance – D&O liability insurance will be allocated based on Total Direct Dollars Assigned to Each Programmatic Function.
Telephone Service - Local telephone service will be allocated based on the Employee Ratio. Long distance calls will be identified with each employee and those charges will be allocated in the same manner as the payroll for each of those employees. A coding feature will track long distance calls for common area telephones.
General Office Supplies - Miscellaneous office supplies will be allocated based on the Employee Ratio.
Copies and Faxes - Copies and faxes will be directly assigned using a coding function on each machine. Common copies and faxes will be allocated based on the ratio of directly assigned copies and faxes.
Accounting and General Financial Services - Accounting and general financial services will be allocated 25% to each program.
Audits - The annual financial audit will be allocated based on the Total Direct Dollars Assigned to Each Programmatic Function. Programmatic audits as discussed above will be directly assigned.
Legal and Regulatory - These costs will be allocated based on the Total Direct Dollars Assigned to Each Programmatic Function. Specific project work, however, will be directly assigned.
Billing and Collection Expenses - Billing and collection costs are currently and will continue to be allocated 25% to each program.
Website - Website costs will be allocated based on the Relative Number of Visits to the Website. Any special developmental costs associated with a specific program will directly assigned.
Vendor Outreach - Outreach that is beneficial to more than one program will be allocated based on Total Direct Dollars Assigned to Each Programmatic Function that is benefited.
Miscellaneous - All other common costs that are not included above will be allocated 25% to each mechanism.

Assets and Liabilities
Assets and Liabilities will be directly assigned to each programmatic function. Assets and liabilities that are common in nature will be allocated 25% to each program.

USAC will consolidate its accounting, general ledger, payroll, and time-reporting systems on January 1, 1999. These systems will support the above cost allocation procedures.